

## Federal Reserve System

## § 250.248

### **§ 250.246 Applicability of section 23A of the Federal Reserve Act to the purchase of a security by an insured depository institution from an affiliate.**

(a) The purchase of a security by an insured depository institution from an affiliate that is a broker-dealer registered with the Securities and Exchange Commission is exempt from section 23A of the Federal Reserve Act (12 U.S.C. 371c) under paragraph (d)(6) of that statute if:

(1) The security has a “ready market,” as defined in 17 CFR 240.15c3-1(c)(11)(i);

(2) The security is eligible for a State member bank to purchase directly, subject to the same terms and conditions that govern the investment activities of a State member bank, and the institution records the transaction as a purchase of securities for purposes of the bank Call report, consistent with the requirements for a State member bank;

(3) The security is not a low-quality asset;

(4) The security is not purchased during an underwriting, or within 30 days of an underwriting, if an affiliate is an underwriter of the security, unless the security is purchased as part of an issue of obligations of, or obligations fully guaranteed as to principal and interest by, the United States or its agencies;

(5) The security’s price is quoted routinely on an unaffiliated electronic service that provides indicative data from real-time financial networks, provided that:

(i) The price paid by the insured depository institution is at or below the current market quotation for the security; and

(ii) The size of the transaction executed by the insured depository institution does not cast material doubt on the appropriateness of relying on the current market quotation for the security; and

(6) The security is not issued by an affiliate, unless the security is an obligation fully guaranteed by the United States or its agencies as to principal and interest.

(b) The purchase of the security must comply with paragraph (a)(4) of section

23A, which requires that any covered transactions between an insured depository institution and an affiliate be on terms and conditions that are consistent with safe and sound banking practices.

[66 FR 24225, May 11, 2001]

### **§ 250.247 Application of sections 23A and 23B of the Federal Reserve Act to derivative transactions between insured depository institutions and their affiliates.**

(a) Derivative transactions between an insured depository institution and its affiliates are subject to the market terms requirement of section 23B(a)(1) of the Federal Reserve Act (12 U.S.C. 371c-1(a)(1)).

(b) An insured depository institution must establish and maintain policies and procedures reasonably designed to manage the credit exposure arising from its derivative transactions with affiliates in a safe and sound manner. The policies and procedures must at a minimum provide for:

(1) Monitoring and controlling the credit exposure arising from the institution’s derivative transactions with each affiliate and all affiliates in the aggregate; and

(2) Ensuring that the institution’s derivative transactions with affiliates comply with section 23B.

(c) For purposes of this regulation, derivative transactions include any derivative contract listed in paragraphs A. III. E. 1. a. through d. of appendix A to 12 CFR part 225 and any similar derivative contract, including credit derivative contracts.

[66 FR 24233, May 11, 2001]

### **§ 250.248 Application of sections 23A and 23B of the Federal Reserve Act to intraday extensions of credit by insured depository institutions to their affiliates.**

(a) Intraday extensions of credit by an insured depository institution to its affiliates are subject to the market terms requirement of section 23B(a)(1) of the Federal Reserve Act (12 U.S.C. 371c-1(a)(1)).

(b) An insured depository institution must establish and maintain policies and procedures reasonably designed to manage the credit exposure arising

from its intraday extensions of credit to affiliates in a safe and sound manner. The policies and procedures must at a minimum provide for:

(1) Monitoring and controlling the credit exposure arising from the institution's intraday extensions of credit to each affiliate and all affiliates in the aggregate; and

(2) Ensuring that the institution's intraday extensions of credit to affiliates comply with section 23B.

[66 FR 24233, May 11, 2001]

**§ 250.250 Applicability of section 23A of the Federal Reserve Act to a member State bank's purchase of, or participation in, a loan originated by a mortgage banking affiliate.**

(a) A question has been raised as to whether a member bank's purchase, without recourse, and at face value, of any mortgage note, or participation therein, from a mortgage banking subsidiary of its parent bank holding company at the inception of the underlying mortgage loan involves a "loan" or "extension of credit" from the member bank to the affiliate within the meaning of section 23A of the Federal Reserve Act (12 U.S.C. 371c). In the given circumstances, the affiliate originated the mortgage loans at premises other than an office of the member bank and hence was not a company furnishing services to or performing services for the holding company or its banking subsidiaries within the meaning of section 4(c)(1)(C) of the Bank Holding Company Act (12 U.S.C. 1843(c)(1)(C)). Loans or extensions of credit to the affiliate were therefore not entitled to exemption from the provisions of section 23A by virtue of subsection (1) of the final paragraph thereof.

(b) Paragraph 4 of section 23A provides that the term *extension of credit* shall be deemed to include the discount of promissory notes, bills of exchange, conditional sales contracts, or similar paper, whether with or without recourse, excepting the acquisition of such paper by a member bank from another bank without recourse. In previously interpreting the statutory provision from which this provision is derived (section 6 of the Bank Holding Company Act of 1956, repealed July 1,

1966), the Board concluded that *discount* in the context of the statute meant *purchase* and that the purchase of notes, bills of exchange, conditional sales contracts or similar paper from an affiliate was subject to the prohibitions of the statute. (1958 Federal Reserve Bulletin 260.) Further, the Board notes that the definition in section 23A is illustrative rather than exclusive. The Board believes that the purposes of section 23A justify a broad construction of the definition of *extension of credit* to include certain purchases of obligations, even though the purchases are not made at a discount from face value. A bank's financing of the working capital needs of a mortgage banking affiliate may occur through outright purchases of obligations, and the types of abuses with which section 23A is concerned are likewise possible in such circumstances, since such transactions between affiliates could result in an undue risk to the financial condition of the purchasing bank.

(c) The Board is of the opinion that the purchase by a member State bank of a mortgage note, or participation therein, from a mortgage banking affiliate would involve a loan or extension of credit to the affiliate if the latter had either made, or committed itself to make, the loan or extension of credit evidenced by the note prior to the time when the member bank first obligated itself, by commitment or otherwise, to purchase the loan or a participation therein. However, there would be no loan or extension of credit by the member bank to its mortgage banking affiliate if the member bank's commitment to purchase the loan, or a participation therein, is obtained by the affiliate within the context of a proposed transaction, or series of proposed transactions, in anticipation of the affiliate's commitment to make such loan(s), and is based upon the bank's independent evaluation of the credit worthiness of the mortgagor(s). In these latter circumstances, the member bank would be taking advantage of an investment opportunity rather than being impelled by any improper incentive to alleviate working capital needs of the affiliate that are directly attributable to excessive outstanding commitments.